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# The Public Service Commission
# State of South Carolina

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November 10, 2004

Public Service Commission of South Carolina
Attention: Docketing Department
P.O. Drawer 11649
Columbia, S.C. 29211

RE: Docket No. 2004-5-G – Annual Review of Purchased Gas Adjustments and Gas Purchasing Policies of South Carolina Electric & Gas Company

Dear Sirs:

Enclosed for filing, please find an original and ten (10) copies of the proposed Order of the Commission Staff in the above-captioned Docket. By copy of this letter, I certify that all parties of record have been served with copies of this proposed Order.

Thank you for your consideration in this matter.

Sincerely,

F. David Butler

F. David Butler
General Counsel

FDB:dd
Enclosure:
cc: All Parties of Record

BEFORE

THE PUBLIC SERVICE COMMISSION OF

SOUTH CAROLINA

DOCKET NO. 2004-5-G - ORDER NO. 2004-

NOVEMBER 10, 2004

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| IN RE: Annual Review of Purchased Gas Adjustments and Gas Purchasing Policies of South Carolina Electric & Gas Company. | ) ) ) ) ) | PROPOSED ORDER OF THE COMMISSION STAFF RULING ON PGA AND GAS PURCHASING PRACTICES |

This matter comes before the Public Service Commission of South Carolina (the "Commission") for the Annual Review of the Purchased Gas Adjustment ("PGA") and the Gas Purchasing Policies of South Carolina Electric & Gas Company ("SCE&G" or "Company"). In addition, pursuant to Order No. 94-1117, the Commission has reviewed the collection of environmental clean-up costs ("ECC") for the relevant period.

The Commission instructed the company to publish a notice (once, in a newspaper of general circulation, in the relevant review areas) advising all interested parties of the manner and time in which to file pleadings to obtain the right to participate in this review. The Commission further instructed SCE&G to provide direct notification of the PGA review to all of its customers affected by the review. The Company provided affidavits to confirm its compliance with the Commission's instructions. Following this notification, the Consumer Advocate for the State of South Carolina ("Consumer Advocate") filed a Petition to Intervene.

On October 21, 2004, the Commission held a hearing in this matter in its offices. The Honorable Randy Mitchell, Chairman, presided. SCE&G was represented by Catherine D. Taylor, Esquire and Francis P. Mood, Esquire. The Consumer Advocate was represented by Elliott F. Elam, Jr., Esquire. The Commission Staff was represented by F. David Butler, General Counsel.

SCE&G presented the testimony of witnesses Martin K. Phalen and Harry L. Scruggs. The Commission Staff presented the testimony of staff witnesses Roy H. Barnette and Brent L. Sires. The Consumer Advocate did not present testimony.

For the reasons stated herein, the Commission finds that SCE&G's purchasing practices for the review period were prudent, and therefore, approves the requested increase in the fuel factor for the coming twelve month period beginning November 2004 and ending October 2005. The new factor of 90.347 cents per therm shall be effective as of the first billing cycle of November 2004.

**Summary of Testimony**

**Mr. Martin K. F Phalen**

Martin K. Phalen, Vice President of Gas Operations for SCE&G, provided testimony regarding the operations and purchasing practices of SCE&G's natural gas distribution system for the review period. He explained that South Carolina Pipeline Corporation had announced plans to merge with SCG Pipeline, Inc. One result of this merger will be that the new entity will be an interstate pipeline, subject to regulation by the Federal Regulatory Energy Commission. Accordingly, it will no longer offer SCE&G bundled service. Therefore, at the effective date of the merger, SCE&G must begin the procurement of its commodity and capacity requirements. Since timing for this merger cannot now be determined, SCE&G states that it may be necessary for the Company to come back to the Commission at some time during the upcoming review period to make any interim adjustments in the Company's purchasing practices and forecasts that may be required. TR. at 7-8.

Mr. Phalen briefly described SCE&G's gas distribution system, which consists of approximately 6,800 miles of mains that carry natural gas to more than 279,000 homes, factories and businesses in 34 of South Carolina's 46 counties. Mr. Phalen stated that because the SCE&G system is geographically diverse, the Company operates and maintains approximately 193 metered delivery points for delivery from South Carolina Pipeline Corporation ("SCPC"), its supplier. The Company relies on SCPC to provide consolidated delivery of supply and to connect the numerous town border stations throughout SCE&G's service territory. TR.at 3.

Mr. Phalen states that, under Commission approved tariffs, SCE&G has contracted with SCPC for a firm contract demand of 276,495 DTS per day. This volume, in addition to SCE&G's two propane air plants, is utilized by SCE&G to serve its core market. Mr. Phalen noted that SCE&G also serves 321 interruptible industrial and commercial customers. TR. at 13-14. These customers have elected to execute interruptible service agreements and have alternate fuels. Mr. Phalen also testified that SCE&G operates and maintains two propane air facilities, which provide critical peak day injections of propane-air into the natural gas distribution system. These facilities serve SCE&G's systems when necessary, and, with contracted demand, provide the company with an effective and reliable supply mix.

Mr. Phalen discussed SCE&G's continuing work to monitor and perform clean-up activities at various environmental clean up sites (with oversight from the EPA and DHEC). He described the Company's cumulative expenses to date as within revised estimates as presented to this Commission in prior PGA proceedings. However, the Company requested that the current ECC rates be maintained.

Mr. Phalen requested approval of a new PGA factor of 90.347 cents per therm. TR. at 17.

Finally, Mr. Phalen testified that SCE&G's purchasing practices are indeed prudent, striking a reasonable balance between reliability and price, and that the ISP-R continues to allow SCE&G to retain interruptible load while improving load factor and reducing system costs. TR at 18.

**Mr. Harry L. Scruggs**

Mr. Harry Scruggs, Senior Rate and Regulatory Specialist in the Gas Rate Department of SCE&G, explained the operation of the Industrial Sales Program (ISP) and discussed the status of the environmental clean up cost factor and the Company's forecasted cost of gas.

Mr. Scruggs testified that all SCE&G customers benefit from SCE&G's use of the ISP because the margins collected help to offset the fixed costs of doing business. He explained that without the ISP-R, SCE&G could not effectively compete against alternate fuel prices. Because of the ISP-R, interruptible customers have remained on the SCE&G

system and have continued to purchase natural gas volumes from SCE&G. Mr. Scruggs opined that these same customers would likely have switched to an alternate fuel absent the ISPR. TR at 40-41.

In addition, margin revenues from interruptible customers cover a portion of SCE&G's fixed costs. Without the competitive sales provided by the ISP-R, more fixed costs would be borne by SCE&G's firm customers. As a result, the margin charged to SCE&G's firm customers (most of which are residential) would be higher. During the period of September 2003 through August 2004, the margin revenues generated by the ISP-R program were over $10,000,000. The ISP customers are able to utilize natural gas as a fuel because of the competitive pricing provision in their contracts. Id.

Mr. Scruggs stated that SCE&G is requesting that the level of the ECC factor remain at 0.8 cents per therm.

Mr. Scruggs then discussed the Company's forecasted cost of gas. The next annual review period begins in November 2004 and ends in October 2005. SCE&G's gas cost forecast begins with the purchasing profile of the historic actual 12-month period ending August 2003. From that point, the company applies the current NYMEX futures prices and then makes adjustments for future known and measurable changes. A projected monthly gas cost was developed and applied to SCE&G's monthly firm forecasted sales.

The Company's forecasted gas cost, plus the prior period true-up, produces an annual levelized PGA of 90.347 cents per therm, which Mr. Scruggs requested this Commission approve. A residential customer using 600 therms would see their annual bill increased by about $16.21 or 2.5%. This purchased gas cost would be incorporated in SCE&G's firm tariff rates for the billing months of November 2004 through October 2005.

**Mr. Roy H. Barnette**

Mr. Roy Barnette, an Auditor with the Commission, testified on behalf of the Commission staff. Mr. Barnette summarized the Audit Staff's findings and stated that Staff had verified SCE&G's gas costs and Environmental Cleanup Costs for the test year ended August 31, 2004. According to Barnette, the cumulative net over-collection, as of October 31, 2004, is $10,813,959. TR. at 73. Barnette also testified that SCE&G was correctly recovering its gas costs pursuant to its approved tariffs.

**Mr. Brent Sires**

Mr. Brent Sires, Chief of Gas in the Commission's Utilities Department, also testified on behalf of the Commission Staff. Mr. Sires presented the Utilities Department's findings and recommendations resulting from its analysis of the Company's gas purchasing policies, Industrial Sales Program, and the cost of gas factor for the period November 2004 through October 2005.

Mr. Sires stated that the Company uses a levelized cost of gas component in its published tariff rates, which allows the Company to project its cost of gas over a twelve month period. On a monthly basis, the Company records (in a deferred or unbilled account) the difference between the cost of gas as collected from its customers and the actual cost of gas incurred by the Company. The Company files monthly reports on this account with the Commission to keep the Commission informed on the activity in that account. The account reflects the net accumulation of over or under collection of gas costs from SCE&G's customers, and the net variance in the account is treated as a true-up provision. The accumulated over or under recovery is recovered or credited in the succeeding twelve month period. TR. at 84-85.

Mr. Sires described the factors contributing to the Company's over-recovery during the review period. The first contributor was the fact that the actual price of the commodity experienced during the review period was less, resulting in an over-collection. TR at 89-90.

Mr. Sires discussed the prudence of SCE&G's use of SCPC and stated that, in the opinion of the Utilities Department, SCE&G receives adequate supplies of firm gas to meet its captive customers' needs and is prudent with regard to its purchases of gas supplies from SCPC. He stated that, in light of the many changes which continue to take place which affect the securing and transportation of gas, SCE&G should continue its ongoing program to ensure that its gas supply is consistent with its customers' needs and to ensure that supply efficiency is maintained at reasonable costs. TR. at 93-95.

Finally, Mr. Sires stated that the operation of the Company's ISP program should continue, since this mechanism allows SCE&G to compete with alternate fuels. TR. at 97-98.

## FINDINGS OF FACT AND CONCLUSIONS OF LAW

Based on the evidence in the record, the Commission makes the following findings and conclusions:

1) We find that SCE&G's gas purchasing practices for the period under review are prudent and that SCE&G has properly recovered its gas costs pursuant to the terms and conditions of the Company's approved tariff. The direct testimony of Company witness Phalen and Staff witness Sires specifically support this conclusion.

Mr. Phalen notes that SCE&G purchases its gas from SCPC under tariffs approved by this Commission. Further, the operation of the SCPC system is backed by much experience among the various members of its knowledgeable Staff. If SCPC becomes an interstate Pipeline and bundled service is no longer available to SCE&G, this Commission may have to reevaluate the Company's purchasing practices.

In support of the Company's position, Staff witness Sires stated that, in the opinion of the Utilities Department, SCE&G receives adequate supplies of firm gas to meet its captive customers' needs and is prudent with regard to its purchases of gas supplies from SCPC. He stated that, in light of the many changes which continue to affect the securing and transportation of gas, SCE&G should continue its ongoing program to ensure that its gas supply is consistent with its customers' needs and to ensure that supply efficiency is maintained at reasonable costs.

We find no evidence in the record to contradict the testimony of Mr. Phalen or Mr. Sires on the issue of SCE&G's prudence regarding its use of SCPC to purchase gas. We specifically find that SCE&G's purchasing practices are prudent and provide a reliable source of reasonably priced gas to meet its customers' needs.

2) The base cost of gas for the coming period shall be 90.347 cents per therm effective beginning with the first billing cycle in November 2004. The testimony of witnesses Scruggs and Sires support this conclusion. The ECC factor shall remain as is.

Mr. Scruggs provided historical data for the review period September 2003 through August 2004 and provided computations for the projected cost of gas per therm for the coming period, September 2004 through October 2005. After all calculations are reviewed, the conclusion is that the base cost of gas should be increased to 90.347 cents per therm. The direct testimony of Staff Witness Sires supports Mr. Scruggs' analysis, and the Commission finds no contradictory evidence in the record.

3) The current industrial sales program shall be continued. The value of this program to the Company's firm customers was discussed by Company witnesses Phalen and Scruggs, and the evidence supporting this finding was uncontroverted. Staff witness Sires also expressed support for the continuance of the program.

4) The tariffs and rate schedules shall be filed reflecting the findings herein within five (5) days of the receipt of this Order by the Company.

5) This Order shall remain in full force and effect until further Order of the Commission.

BY ORDER OF THE COMMISSION:

Randy Mitchell, Chairman

ATTEST:

G. O'Neal Hamilton, Vice Chairman

(SEAL)